Petroleum Tank Release Fund

An analysis of issues surrounding the solvency of the Fund

A report to the Legislative Finance Committee and the Environmental Quality Council

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Petroleum Tank Release Fund Subcommittee
A joint subcommittee of LFC and EQC

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Overview

The Petroleum Tank Release Fund Subcommittee, a joint body of the Legislative Finance Committee and the Environmental Quality Council, met on May 13, 2008 and June 4, 2008 to consider issues surrounding the solvency of the Petroleum Tank Release Fund (the Fund), which posted a $2.4 million shortfall in FY 2007.

The Fund is the default payer for cleanup of releases (spills, leaks) from underground and aboveground petroleum storage tanks, as well as home heating oil tanks. In FY 2008, the Fund continues to fall short in paying for submitted cleanup plans. A total of $5.3 million has been paid in FY 2008, as of April 30, including $1.87 million in deferred payments from FY 2007. Another roughly $2.8 million in submitted plans remains outstanding, while the Fund estimates it has another $5 million in liabilities that has yet to be submitted. These estimates are for tank releases that are *known.* They do not include releases that have yet to be discovered.

This report is a summary of the subcommittee's work and information gathered, thus far. The subcommittee is asking LFC and EQC to review this work and provide direction as to how to proceed. The subcommittee does not feel, at this time, that its purpose is to recommend legislation, but would be willing to do so, if directed. Conversely, the subcommittee feels it could be appropriate for the committees of the whole to review the issues surrounding the Fund's solvency and backlog in payments for cleanups.

The Petroleum Tank Release Compensation Board (the Board), a citizen board that oversees the Fund, has proposed legislative changes for the 2009 Session, as a way to increase revenue and improve the Fund's solvency. These include raising the fuel tax that finances the Fund to a full cent per gallon (currently it's $.0075/gallon) and raising the deductible that tank owners and operators pay to the Fund for their portion of cleanup costs when a release occurs. The subcommittee has taken no position on any of these proposals.

The subcommittee has also learned that the Fund has agreed to participate in a voluntary audit of 14 state petroleum cleanup programs by the U.S. Environmental Protection Agency this year. The involved programs represent those with the largest backlog of cleanups in the country, or the greatest percentage backlog in their region, as is the case for Montana.

Findings

Task: Examine the backlog in payments from the Petroleum Tank Release Fund for cleanup at petroleum release sites

Finding 1: Petroleum tank owners and operators rely on the Fund as the default payer for cleanups, instead of the payer of last resort.

Finding 2: Payments are limited to available Fund revenue, generated by a $.0075/gallon fuel tax. The tax does not generate enough revenue to cover all existing cleanup plans.

Finding 3: The backlog is caused by an inability to resolve (or close) cleanups at many release sites where the Department of Environmental Quality requires long-term monitoring of groundwater and soil contamination. Those obligations and the cost of ongoing monitoring stress the Fund and reduce its ability to deal with other petroleum releases.

Finding 4: The Fund is using a prioritization system to pay for cleanups at the most hazardous sites first; lower priority sites languish, unable to be closed.

Finding 5: There is disagreement between industry, the Board, and the DEQ as to the extent that cleanups should occur, in order to facilitate site closures.

Finding 6: The U.S. Environmental Protection Agency encourages states to use a "risk based" approach in cleaning up petroleum releases, allowing contaminants to remain in the soil or groundwater, if they pose no risk of spreading or causing harm.

Finding 7: Montana currently uses a "risk based" approach to develop site cleanup plans, but not for site closure, where contaminants could remain in the ground without further monitoring.

Finding 8: Revenue from the existing fuel tax is likely to decline, as motorists reduce their consumption in response to rising fuel prices. For that same reason, it's unlikely that the Legislature would pass a fuel tax increase, as proposed by the Board.

Finding 9: Montana is not ready to transition to a system that requires tank owners and operators to obtain private insurance to pay for petroleum cleanups. Experience with private insurance has been mixed in other states, where some insurers are declining to cover petroleum releases, or take long periods of time to pay claims.

Finding 10: Increasing the deductibles that are applied to cleanups paid by the Fund, as proposed by the Board, would result in higher out-of-pocket costs or insurance premiums for tank owners and operators.

Background

The subcommittee was formed as a joint body of the Legislative Finance Committee and the Environmental Quality Council, which have both heard reports in the past about the solvency of the Fund. There has been general concern for several years about the future of the Fund, which was the subject of a legislative audit, published in November 2003. The audit recommended that Montana transition from reliance on the Fund to private insurance coverage. The audit said the Legislature could consider options that would ease the transition, including an interim reinsurance/excess coverage program. To date, this has not occurred. Ten other states have transitioned to private insurance.[1]

National snapshot of state cleanup funds

Montana is not alone in its difficulty. Nine states have cleanup funds for which outstanding claims exceed the available account balance.[2]

Owners of federally regulated underground storage tanks are required by the U.S. Environmental Protection Agency to have the financial means ($1 million) to help pay for cleanup costs and third party damages caused by a release from their tank. Federally regulated tanks include those (and their connecting pipes) with a capacity greater than 110 gallons. They do not include home heating oil tanks and farm or residential tanks with a capacity of less than 1,100 gallons used for non-commercial purposes. While exempt from federal regulation, those kinds of tanks are, under Montana statute, eligible to be covered by our Fund, if a release occurs.

Private insurance, self-insurance, bonding and other resources can be used by tank owners and operators to comply with the EPA's $1 million "Financial Responsibility" requirement. State funds, whose operations are approved by the EPA, like Montana's, also qualify as evidence of Financial Responsibility. State funds have been the primary source of doing so since the late 1980s. At that time, many state funds were created due to what was seen as a lack of available and affordable private insurance options, especially for "mom and pop" gas stations, and a desire to keep petroleum cleanups moving forward.

Since the mid-1990s, the national backlog of cleanups has been consistently declining from a high of 171,795 sites in 1995 to 108,766 at the end of FY 2007.[3] However, the number of cleanups being completed each year is also declining.[4] Last year, EPA began an effort to better

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[1] Summary of State Fund Survey Results, conducted by the Vermont Department of Environmental Conservation, May 2007.

[2] Ibid.

[3] "Addressing the cleanup backlog: Phase 2 Study," EPA, page 1.

[4] Ibid, page 2.

understand the reasons behind the backlog. EPA's initial work found that 54% of all backlogged sites are over ten years old (in Montana it's 55% [5]) and that many sites in the backlog are either owned or affiliated with a few "brand name" companies.[6] EPA says this suggests that by focusing on older sites or brand name companies, among other things, there may be opportunities for developing targeted strategies to address the backlog.

EPA is continuing its audit this year, by looking more closely at the 14 states with the largest backlogs in the country, or the greatest percentage backlog in their region, as is the case for Montana. Montana has a 50% backlog, according to Janice Pearson, Underground Storage Tank Team Leader for the EPA Region 8 Office. The audit is voluntary and DEQ and the Fund have agreed to participate. EPA hopes this "Phase 2 Study" will further characterize backlogs in individual states, as well as help develop national and state-specific strategies to overcome obstacles and accelerate cleanups.[7]

Snapshot of Montana's Situation

When a petroleum release happens in Montana, the cleanup process generally follows the chronological order outlined in Appendix A, a flowchart published by DEQ, recognizing that variations can occur, depending on individual site characteristics.

As of May 7, 2008, a total of 4,414 releases have been identified in Montana since the Fund came into existence nearly two decades ago. Of those, 2,708 have been resolved, 1,706 remain active.[8] Historically (1990-2007), Montana has averaged 90 site closures per year. But between 2005 and 2007 that average has dropped to 30.[9] Thus far in calendar year 2008, 39 sites have been evaluated for closure; 31 have been approved.[10] Montana's most prolific cleanup year was 1995 with 555 sites closed.[11]

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[5] "Montana Backlog Background," EPA, June 4, 2008.

[6] "Addressing the cleanup backlog: Phase 2 Study," EPA, page 3.

[7] Ibid.

[8] DEQ Petroleum Technical Section Activity Report, May 7, 2008.

[9] "Montana Backlog Background," EPA, June 4, 2008.

[10] DEQ Petroleum Technical Section Activity Report, May 7, 2008.

[11] "Montana Backlog Background," EPA, June 4, 2008.

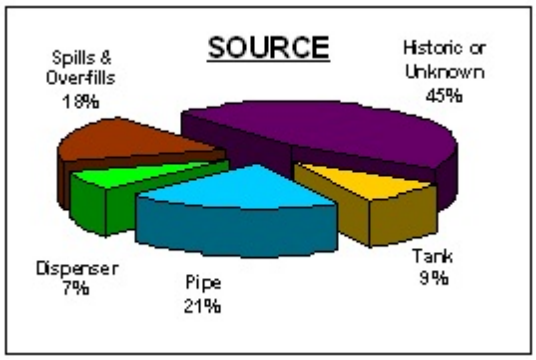

Figure 1: The sources of petroleum releases discovered in 2007, according to DEQ.

New Releases

In 2007, Montana identified 67 new petroleum releases, 83% of which involved gasoline or diesel products. These discoveries follow the trend over the past several years, in which between 50 and 70 new releases were discovered each year.[12]

Historic contamination remains the primary source of new releases, accounting for 39% last year. (Historic and unknown sources combine for 45% in Figure 1.) Historic contamination is mainly discovered through environmental assessments or unrelated construction activities, according to DEQ. The agency also says such releases don't provide much information to help prevent future releases, because most of the historical contamination originated from older tanks systems that were constructed, installed, and operated much differently than the current equipment in service today. DEQ expects historic contamination will continue to make up a significant proportion of newly discovered releases. However, the agency says there are a finite number of unknown historic contamination sites out there; so as they're found, their significance will decline over time.

DEQ has identified piping components as the weak link in active tank systems. Retrofitting existing tank systems with secondary containment and inspecting existing secondary containment can help prevent releases to the environment.[13] DEQ says educating gas station employees and the public could also reduce the number of spills and overfills.

Revenue Generation

The Montana Petroleum Tank Release Fund is currently financed with a $.0075/gallon fuel tax that has generated more than $6 million in revenue annually since 2000. Revenue is expected to decline given the state of the market, as motorists reduce consumption. Fund expenditures have varied between $5.5 million and $9.4 million since 2000, including an average of $1.6 million in annual administrative costs that come directly out of the Fund and are not paid by General Fund money.

The citizen board that oversees the Fund has proposed legislative changes to improve the Fund's solvency. These include raising the fuel tax to a full cent per gallon and obligating administrative costs to the General Fund or another revenue source. The Board also proposes increasing the deductible that owners and operators pay when a leak occurs from $17,500 per incident to $25,000 per incident, plus 5 % of the total bill between $50,000 and $1,000,000. The

[12] "Release Autopsies -- 2007," DEQ.

[13] Ibid.

Board feels this would encourage greater use of private insurance. The subcommittee has taken no position on any of these proposals.

Due to the Fund's financial strain, a prioritization system has been developed to cleanup what are considered to be the most hazardous sites first. However, that leaves less funding available for lower-priority sites that may be closer to wrapping up.

Private Insurance

Current use of private insurance appears to be limited, with the Fund remaining the default payer for many cleanups at petroleum release sites. With mixed experience in other states, where some insurers are declining to cover petroleum releases, or take long periods of time to pay claims, the subcommittee does not feel Montana is ready to transition to a system that mandates use of private insurance for all tank owners and operators. Even when an insurance policy exists, some tank owners and operators acknowledge they don't report releases to the insurer, but instead seek payment for cleanup directly from the Fund.

According to data collected through the state's permitting system for federally regulated underground storage tanks, 1,340 tank owners and operators in Montana report they have some mechanism in place to meet the federal Financial Responsibility requirement of $1 million. Most notably, 522 claim self-insurance, 341 report they have private insurance, and 781 rely on the Fund to show Financial Responsibility. A small number of others use mechanisms such as surety bonds, letters of credit, and trust funds.

Collecting payment from private insurance can be complicated, given a property owner may have purchased policies from multiple providers over the years, or a historically contaminated property may have changed hands one or several times before the release is discovered. The Fund uses a third party to ferret out these channels of payment, a process referred to as subrogation. Depending on how the money is recovered (by settlement, through trial), the third party is paid 22-25% of the recovered amount for its services, plus a $70/hour fee.

Of the top 21 most expensive petroleum releases in Montana (costing more than $500,000 to cleanup), three did not have insurance, the cause of five others was undetermined and therefore an insurer was unlikely to pay for cleanup, and 12 others went to subrogation. These top 21 releases were discovered between October 1989 and April of 2000.

It appears the Board did not actively seek to recover cleanup costs from insurance companies for any release until about six years ago. Several of those attempts have since gone to litigation. In 2006, the Montana Supreme Court ruled that the statute of limitations that applies to these cases is eight years and the clock begins running at the time that the release is discovered. In the 2006 case, the Board was seeking to recover $254,842 in cleanup costs from the insurer of a gas station in Butte. The release was discovered in 1989. The Board didn't submit a claim to the insurer until 2001. The court ruled that was well after the statute of limitations had expired and the insurer didn't have to pay. The Board sought to have the ruling overturned. On June 3, 2008,

the Montana Supreme Court affirmed its 2006 ruling, again stating that the eight year statute of limitations applies and the clock begins at the time a release is discovered.

Given these rulings, it appears the Board may no longer seek insurance payments on any of the top 21 most expensive releases (to date). It is unclear how many other releases may also be too old to seek repayment from insurance. Allan Payne, subrogation attorney for the Board, estimates there could be $10 million in now-unrecoverable costs. Mr. Payne says the Board is currently evaluating releases from July 2000, to ensure that it files any necessary claims before the statute of limitations runs out on those cases this month. The Board didn't take similar action after the first ruling in 2006, choosing instead to try to have the ruling overturned.

Extent of cleanups

There is disagreement between industry, the Board, and the Department of Environmental Quality as to the extent that cleanups should occur. (The DEQ must approve the work plan for the cleanup of each release.) The DEQ says Montana has stricter statutory and constitutional environmental standards than many states, which must be met before a site can be considered "cleaned up" and closed. Industry argues that DEQ has made its own "policy" decisions to follow more stringent protocols than required by statute and the Constitution. The Board feels "lesser" cleanups could be possible to facilitate more efficient and cost-effective site closures. The subcommittee hasn't resolved the differences in these opinions.

In Article II, Section 3, the Montana Constitution grants state residents the inalienable right to a clean and healthful environment. The Montana Supreme Court has defined this fundamental right, paraphrased as follows:

> The constitutional right to a clean and healthful environment includes being free from unreasonable degradation (significant impact on the environment)...and this right is anticipatory and preventative in nature. [14]

This does not mean, however, that there cannot be any adverse change to the environment. The Montana Supreme Court has also held that the environmental provisions of the Constitution apply not only to state actions, but also private actions and therefore private parties.[15]

In statute, the provisions of Title 75, chapter 5, provide regulatory guidance regarding prevention, abatement and control of the pollution of Montana waters.[16] Water quality laws govern only certain state waters, including surface or underground bodies of water, irrigation systems, or

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[14] MEIC v. DEQ, 296 Mont. 207 (1999)

[15] Cape- France Enterprises v. the Estate of Lola H. Peed, 2001 MT 139* (2001)

[16] Great liberty has been taken here in terms of lifting much of the explanation of the Water Quality Laws under this section literally verbatim from the EQC Water Quality Handbook (2008).

drainage systems.[17] Montana water quality laws regulate every entity in the state, including individuals, businesses, organizations, and units of government. However, water quality laws only regulate certain uses, including entailing potential pollution (either point source or non-point source).

For further discussion of statutory and constitutional requirements pertaining to site remediation and closure, please refer to Appendix B.

The DEQ says it can't close petroleum release sites until they meet drinking water standards, as prescribed in the technical document known as Circular DEQ 7, "Montana Numerical Water Quality Standards." These standards were developed in accordance with the Montana Water Quality Act and the Federal Clean Water Act, with guidance from the EPA. The standards are updated as additional information or guidance from the EPA becomes available.[18]

The DEQ says it understands the burden that long-term groundwater monitoring, used at many cleanup sites, can put on the Fund and the frustration it can cause for property and tank owners, who'd like to see their cleanup resolved. The DEQ says it's looking more closely at closing sites where contaminants could be left in the ground, if they pose no risk of spreading or causing harm. This is called "risk based site closure."

The EPA has recommended this risk based approach since the 1990s. EPA recently told the Montana DEQ that the approach has been used in other states to effect faster and cheaper cleanups, while still protecting human health and the environment.[19] Montana is using risk based assessments in developing cleanup plans for contaminated sites, but not for site closure. Industry and the Board say to address Montana's backlog, it'll be necessary to leave contaminants in the ground where possible. Industry says it won't support the proposal to increase the deductibles that tank owners and operators pay as part of state-funded cleanups, unless DEQ alters its protocols.

[17] 75-5-103(29)(a), MCA

[18] Circular DEQ 7, February 2006, http://www.deq.mt.gov/wqinfo/Circulars.asp

[19] Letter from Janice Pearson, EPA Region 8 UST Team Leader to Michael Trombetta, chief of the Hazardous Waste Site Cleanup Bureau at the Montana Department of Environmental Quality, June 4, 2008.